National Energy Board | Office national de l'énergie

Reasons for Decision

Canadian Association of Petroleum Producers

RH-R-1-2005

May 2005

Review of RH-2-2004 Phase I Decision

Canada

National Energy Board

Reasons for Decision

In the Matter of

Canadian Association of Petroleum Producers

Application dated 12 November 2004
requesting a review of Board Decision
RH-2-2004 Phase I

RH-R-1-2005

May 2005

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Cat No. NE22-1/2005-4E
ISBN 0-662-40533-1

This report is published separately in both official languages.

Copies are available on request from:
The Publications Office
National Energy Board
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Calgary, Alberta, T2P 0X8
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For pick-up at the NEB office:
Library
Ground Floor

Printed in Canada

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N° de cat. NE22-1/2005-4F
ISBN 0-662-74134-X

Ce rapport est publié séparément dans les deux langues officielles.

Demandes d'exemplaires :
Bureau des publications
Office national de l'énergie
444, Septième Avenue S.-O.
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Des exemplaires sont également disponibles à la bibliothèque de l'Office
(rez-de-chaussée)

Imprimé au Canada

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Recital and Appearances

IN THE MATTER OF the *National Energy Board Act* and the regulations made thereunder; and

IN THE MATTER OF an application dated 12 November 2004 by the Canadian Association of Petroleum Producers pursuant to subsection 21(1) of the Act for a review of National Energy Board Decision RH-2-2004 Phase I; and

IN THE MATTER OF Proceeding RH-R-1-2005.

Heard in Calgary, Alberta on 26 April 2005.

BEFORE:

K.W. Vollman	Presiding Member
E. Quarshie	Member
C. Dybwad	Member

Appearances:

D. G. Davies	Canadian Association of Petroleum Producers
T. Lange	Coral Energy Canada Inc.
C. K. Yates, Q.C.	TransCanada PipeLines Limited
M.A. Fowke L.C. Bell	National Energy Board

Chapter 1

Introduction

On 12 November 2004, the Canadian Association of Petroleum Producers (CAPP) applied pursuant to subsection 21(1) of the *National Energy Board Act* and section 44 of the *National Energy Board Rules of Practice and Procedure, 1995* (Rules) for a review of National Energy Board Decision RH-2-2004 Phase I[1] (Phase I Decision) on the basis that the Board committed errors with respect to Non-Renewable Firm Transportation (FT-NR), long-term incentive compensation (LTIC) and regulatory costs.

By letter dated 15 December 2004, the Board established a process to solicit comments on the first step of the review. Comments in support of CAPP's application were received from Cargill Power & Gas Markets (Cargill); the Industrial Gas Users Association (IGUA); Coral Energy Canada Inc. (Coral) and the Cogenerators Alliance (CA); Union Gas Limited (Union); and, le Procureur général du Québec (Quebec). TransCanada PipeLines Limited (TransCanada) filed comments opposing the CAPP application and, with the agreement of CAPP, filed supplemental comments responding to parties supporting the CAPP application. CAPP subsequently filed reply comments.

After considering the comments of all parties, the Board issued a letter dated 18 February 2005 dismissing the CAPP application on the regulatory costs ground of review. With respect to FT-NR, the Board found that CAPP had raised a doubt as to the correctness of the Board's decision and sought comments on the process for step 2 of the review. The Board did not address the LTIC ground of review as a result of the CAPP letter of 11 February 2005 requesting that the Board defer its consideration of that ground pending further advice. The LTIC ground of review was subsequently withdrawn by CAPP on 13 April 2005.

The Board considered the submissions on process received from CAPP, TransCanada, IGUA and Union, and by letter dated 18 March 2005, set step 2 of the review on FT-NR down for an oral public hearing as proceeding RH-R-1-2005. By separate letter of the same date, the Board sought additional information from TransCanada. TransCanada filed its response to the Board's request for information on 14 April 2005. The Board received written argument from IGUA on 6 April 2005 and from Union on 25 April 2005. Oral argument was heard from CAPP, Coral and TransCanada on 26 April 2005 in Calgary.

1 TransCanada PipeLines Limited, RH-2-2004, Phase I, Tolls and Tariff, September 2004.

Chapter 2

FT-NR

2.1 Background

By early 2004, TransCanada had contracted capacity commencing in the future for a segment of its pipeline, but recognized that demand existed for that capacity in the interim time period. TransCanada had the option of offering the interim capacity through Interruptible Transportation (IT) or Short Term Firm Transportation (STFT), but was of the view that there was an opportunity to contract the interim capacity on a longer-term basis than what would be allowed by STFT, and on a firmer basis than what would be allowed by IT.

TransCanada could not, however, offer the capacity on a long-term firm basis under its standard FT contract because of the renewal provision contained within Article 8 of TransCanada's FT Toll Schedule and incorporated by reference into the FT contract. Article 8 grants a shipper the option to renew the contract for a period no less than one year at a contract demand level no greater than that set out in the contract. Since the capacity in question was already pre-committed to a future date, inclusion of the option to renew the interim capacity would not be workable.

Following discussions with shippers, TransCanada circumvented this problem by altering Article 2.1 of the *pro forma* FT contract contained within its tariff to include a mandatory condition by which contracted volumes would be stepped-down to zero prior to a certain date. The effect of the step-down is that the FT contract renewal provision would apply to zero volumes, thereby ensuring that the required capacity would be available to fulfill the previously-assigned contract in the future. TransCanada offered this service through a February 2004 open season at the 100% Load Factor FT toll. TransCanada did not seek Board approval of the amendment of the *pro forma* FT contract to step-down to zero volumes, nor did it seek Board approval to charge the FT toll for this service.

In its 2004 Mainline Tolls and Tariff Application, TransCanada applied for approval of a new service known as FT-NR. This service was proposed by TransCanada as a unique, non-renewable and biddable service that could be used to market term-limited blocks of capacity when TransCanada has already committed to firm service commencing more than one year in the future. The Board heard all elements of the 2004 Application, other than cost of capital, in the RH-2-2004 Phase I Proceeding.[2]

In the Phase I Decision, the Board approved the FT-NR service. It stated:

> Although the evidence indicates that such capacity could be offered to the market through the use of FT contracts with a step-down provision, the Board is of the

2 Cost of capital was heard in the RH-2-2004 Phase II Proceeding. The Board's Reasons for Decision on Phase II were issued in April 2005.

> view that a specific discrete service [i.e., FT-NR], with clear terms and conditions, is preferable.[3]

Further, the Board approved the toll for FT-NR to be determined on a biddable basis with a floor-price equal to the 100% Load Factor FT toll. It found that FT-NR would be traffic that does not flow under substantially similar circumstances and conditions to FT; that approving the service on a biddable basis would ensure allocative efficiency and contribute to overall economic efficiency; and, that approving a biddable FT-NR service would not constitute an erosion of the cost-based approach to the determination of FT tolls.

2.2 Step 1 of the Review

In step 1 of the review, the Board must make a determination pursuant to subsection 45(1) of the Rules as to whether the Phase I Decision ought to be reviewed. The test is whether CAPP has raised a doubt as to the correctness of the Decision.

Position of CAPP

In its application for review, CAPP alleged that the Board erred in the Phase I Decision by approving tolls for FT-NR that would be determined on a biddable basis.

CAPP submitted that FT-NR would be traffic that flows under substantially similar circumstances and conditions to FT with a step-down. Both services could be used to market term-limited blocks of capacity. Further, a contract with no renewal provision (i.e., FT-NR) is equivalent to a contract renewable at zero volumes (i.e., FT with a step-down). Accordingly, in CAPP's submission, it was not open to the Board to approve a different toll for FT-NR than the cost-based FT toll applicable to FT with a step-down.

CAPP further submitted that the cost-based FT toll is the appropriate toll to be charged for FT-NR. Citing *TransCanada PipeLines Limited v. National Energy Board et al.*,[4] CAPP asserted that the Board has determined that the just and reasonable toll model for the Mainline is cost-based, and having made that determination, the Board must "faithfully adhere" to the model.

Positions of Parties in Support of CAPP

IGUA submitted that the Board committed errors of law by making findings unsupported by the evidence. Specifically, IGUA stated that the Board did not have evidence to support its findings that FT-NR is a unique service substantively different from FT with a step-down, nor that FT-NR would be traffic that does not flow under substantially similar circumstances and conditions to FT. IGUA also submitted that, as the services are substantially the same, the Board was prohibited by section 62 of the Act from treating FT-NR and FT with a step-down differently for toll-making purposes.

Union stated that the Board's approval of a biddable toll for FT-NR was fundamentally incorrect. It noted that biddable tolls have to this point been restricted to short-term and discretionary

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3 *Supra* note 1 at 28.

4 2004 FCA 149 [hereinafter *TransCanada*].

services. Union stated that the Board provided two reasons for departing from cost-based tolls for FT-NR. The first is that FT-NR is different than FT. Union submitted that the differences between the two services cited by the Board may have justified a different cost-based toll for FT-NR, but they did not justify a departure from the cost-based toll methodology. The second is that biddable tolling enhances allocative efficiency. Union's position was that making the toll for any service biddable enhances allocative efficiency and that this would not, therefore, be a reason for making any particular service biddable.

Quebec indicated its support for the grounds raised in CAPP's application for review but did not comment on the FT-NR issue specifically. Comments received on step 1 from Cargill and Coral and CA were restricted to the LTIC issue.

Position of TransCanada

TransCanada submitted that the Board clearly found that FT-NR would be traffic that does not flow under substantially similar circumstances and conditions to FT, and that the difference in traffic justifies a difference in tolls. TransCanada stated that the issue in the Phase I Proceeding was whether the toll for FT-NR could and should differ from the toll for FT service. What was not in issue, in TransCanada's submission, was whether the toll for FT-NR should differ from the toll for FT with a step-down, or whether FT with a step-down should be tolled the same as FT. TransCanada stated that FT with a step-down is a service which it will likely not offer again, noting that its evidence in the Phase I Proceeding was that FT with a step-down was an interim solution pending approval of FT-NR. In TransCanada's submission, if CAPP wants the Board to decide on the appropriate tolling for FT with a step-down, CAPP can make an application to the Board for that determination.

In terms of the biddable feature of FT-NR, TransCanada disputed CAPP's assertion that following the *TransCanada* case, the Board must "faithfully adhere" to the cost-based model, noting that the Board is not required to adopt any particular methodology, including a cost of service methodology. TransCanada further stated that if CAPP's assertion was true, there could be no biddable services or incentive settlements.

In its supplemental comments, TransCanada took issue with Union's position that the enhancement of allocative efficiency is not relevant to whether a toll should be biddable. TransCanada noted that Union made this argument at the Phase I Proceeding and that the Board must be presumed to have considered that argument, as well as the arguments of other parties, before making its decision. TransCanada further submitted that Union was effectively taking the position that the Board cannot approve any biddable services.

Reply of CAPP

In response to TransCanada, CAPP stated that the Board made two errors with respect to FT-NR. First, CAPP stated that the Board erred by approving a different toll for FT-NR than the toll for FT with a step-down, which is contrary to section 62 of the Act. CAPP noted that TransCanada did not dispute that FT-NR and FT with a step-down provide the same service, are substantially similar traffic and should be charged the same toll. Rather, CAPP submitted, TransCanada only stated that FT with a step-down was not in issue in the Phase I Proceeding and that CAPP could

have raised the issue then if it so chose. In response, CAPP explained that it was in agreement with the cost-based FT toll being charged for FT with a step-down and therefore had no reason to take issue with it during the Phase I Proceeding.

Second, CAPP alleged that the Board erred in concluding that the differences between FT-NR and FT justify biddable tolling for FT-NR. CAPP reiterated that, having established a cost-based toll for the Mainline, there is a legal necessity to adhere to this methodology in providing long-term firm service such as FT-NR. This legal requirement could not, in CAPP's submission, be overridden by the pursuit of allocative efficiency.

In addition, CAPP disputed the statement made by TransCanada that faithful adherence to a cost-based regulatory model would mean that there could not be any biddable services. CAPP stated that the established regulatory model permits biddable tolls for short-term or other discretionary services, but argued that FT-NR is neither a short-term nor a discretionary service.

Views of the Board

The Board's letter dated 18 February 2005 contains the Board's determination that the Phase I Decision ought to be reviewed on the question of whether the Board erred in approving a different toll for FT-NR than the FT toll charged for FT with a step-down.

The Board did not proceed to a review on the question of whether the original Panel erred in departing from cost-based tolls for FT-NR. While not set out in the 18 February 2005 letter, the Board's reasons for that determination are as follows. On the first step of review, the Board's responsibility is not to apply its own judgment and opinion to the matter. Rather, its task is to determine whether an applicant for review has raised a doubt as to the correctness of the decision.[5] The Board is of the view that, even when using a cost-based toll methodology, it is open to it to find that a particular service could be tolled under a methodology other than cost-based tolls. The original Panel had the discretion, therefore, to exercise its informed judgment and opinion to determine that biddable tolling would result in just and reasonable tolls. Accordingly, the Board was not persuaded that CAPP had raised a doubt as to the correctness of the Phase I Decision on the basis that the Board erred in departing from cost-based tolls for FT-NR.

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5 See TransCanada PipeLines Limited, RH-R-1-2002, Review of RH-4-2001 Cost of Capital Decision, February 2003 at 5.

2.3 Step 2 of the Review

As noted above, the Board proceeded to a review on the question of whether the Board erred in approving a different toll for FT-NR than the FT toll charged for FT with a step-down. In step 2 of the review, the Board is required to make a determination as to whether the Phase I Decision regarding the tolling of FT-NR should be confirmed, amended or overturned. Further, if the Board decides to amend or overturn the Phase I Decision, the Board must decide on the appropriate tolling methodology for FT-NR.

Position of CAPP

CAPP stated that section 62 of the Act precludes TransCanada from charging different tolls for the same service. In CAPP's submission, FT-NR and FT with a step-down are the same service. Both have firm priority, can be used to access term-limited blocks of capacity and are effectively non-renewable. CAPP argued that the evidence presented in the Phase I Proceeding established that the two services are substitutable, with the only distinction being that there is greater administrative burden associated with FT with a step-down than with FT-NR.

Since FT-NR and FT with a step-down flow under the same circumstances and conditions, CAPP stated that the two services must be charged the same toll. CAPP noted that the Phase I Decision does not address the issue of the lawfulness of charging a different toll for FT-NR than that charged for FT with a step-down. In CAPP's submission, the Phase I Decision must be varied and the Board must conclude that the approved toll for FT-NR is the cost-based FT toll.

CAPP further took issue with the distinction TransCanada appears to draw between FT with a step-down to a volume greater than zero and FT with a step-down to zero. In CAPP's submission, there is no basis for such a distinction for tolling purposes since the amount that is non-renewable in either contract should be tolled the same. Noting that the cost-based toll is considered to be the just and reasonable toll for FT without a step-down and for FT with a step-down to a volume greater than zero, CAPP argued that the cost-based toll must also be the just and reasonable toll for FT with a step-down to zero and for FT-NR.

In addition, CAPP submitted that TransCanada clearly considered the FT toll to be the just and reasonable toll for FT with a step-down when it offered service under contracts at that toll through to March 2006. CAPP disputed TransCanada's assertion that the utilization of FT step-down contracts in 2004 was an interim solution that was not meant to establish a precedent. CAPP stated that the CAPP and Coral and CA evidence in the Phase I Proceeding was that FT-NR was unnecessary because the same service could be provided by FT with a step-down. Further, CAPP stated that the evidence of TransCanada was that step-down service would be offered again if requested by a shipper and CAPP assumed it would continue to be offered at the FT toll.

Positions of Parties in Support of CAPP

In an oral submission, Coral supported the arguments put forward by CAPP. Coral submitted that there is no difference in service to justify charging higher tolls for FT-NR. Coral argued that all long-term capacity available on the Mainline, including renewable FT, FT with a step-down

and FT-NR, should be charged the cost-based FT toll. Coral further disputed the claim that a biddable price for FT-NR is required for efficient allocation of capacity. In addition, Coral stated that, in its view, TransCanada was operating within its tariff when it offered FT with a step-down service.

IGUA submitted that the Board incorrectly approved a biddable, rather than a cost-based, toll for FT-NR. It stated that FT with a step-down and FT-NR are substantially the same services and that the Board is prohibited from treating them differently for tolling purposes pursuant to section 62 of the Act. IGUA further asserted that there was no evidence of any probative value to support the Board's characterization of FT-NR service as a "specific discrete" or "unique" service or to support its finding that "FT-NR would be traffic that does not flow under substantially similar circumstances and conditions to FT". In addition, IGUA stated that FT-NR is a firm service, rather than a short-term or discretionary service, and should be tolled on a cost basis like FT and FT with a step-down.

Union argued that the Board's decision to approve biddable tolling for FT-NR was fundamentally incorrect. It submitted that the differences between the characteristics of FT and FT-NR do not warrant a departure from cost-based tolls for FT-NR. Further, in Union's submission, allocative efficiency alone cannot justify making a toll biddable.

Position of TransCanada

TransCanada submitted that the fact that FT step-down contracts exist at the FT toll should not be dispositive of the legality of biddable FT-NR for two reasons.

First, in TransCanada's submission, FT with a step-down and FT-NR are not traffic of the same description transported under substantially similar circumstances and conditions. Citing the RH-1-88 Phase II Decision,[6] TransCanada argued that the Board may take into account the business motives of the parties and the circumstances and conditions created by contract when determining, as a question of fact, whether traffic is carried under substantially similar terms and conditions. Given the evidence in the Phase I Proceeding that FT with a step-down was an interim solution designed to take advantage of a market opportunity and to respond to shipper demand for capacity while TransCanada sought approval of biddable FT-NR, TransCanada submitted that the two services constitute different traffic. Accordingly, TransCanada argued that the Board did not err in approving a toll for FT-NR that could differ from the toll charged for FT with a step-down and that the Phase I Decision should be confirmed.

Second, TransCanada noted that it had not sought Board approval of FT with a step-down. TransCanada stated that in its view, the tariff and other regulatory authority neither specifically authorized it to nor forbid it from amending the *pro forma* contracts to allow a step-down to zero. TransCanada asserted that the existence of FT contracts with a step-down provision at the FT toll, which was neither considered nor approved by the Board, could not and should not be used to conclude that the adjudicated approval of biddable FT-NR was an error of law. It argued that

6 TransCanada PipeLines Limited, RH-1-88, Phase II, Tolls, June 1989 at 46 to 48.

a filing under paragraph 60(1)(a) of the Act should not trump an adjudicated disposition under paragraph 60(1)(b) of the Act.[7]

Reply of CAPP

CAPP disputed TransCanada's assertion that FT with a step-down and FT-NR are not traffic of the same description transported under substantially similar circumstances and conditions. CAPP stated that the services are substitutable and are intended to satisfy the same market demand. In CAPP's submission, FT with a step-down was not an interim measure to be used only until FT-NR received approval, noting that the evidence in the Phase I Proceeding was that FT with a step-down may be provided in the future and in fact would be provided if requested by a shipper.

CAPP further argued that the issue on review should not be about one toll trumping another toll; it should be about charging the same toll for the same service. CAPP stated that TransCanada's own evidence in the Phase I Proceeding was that the FT toll would not be unjust and unreasonable for FT-NR.

In CAPP's view, TransCanada did not contravene the wording of its tariff by offering FT with a step-down and by charging the FT toll for that service; however, CAPP stated that the contracts may have infringed the spirit of the tariff's renewal provision.

Views of the Board

In order to determine whether the Board's decision regarding the tolling of FT-NR should be confirmed, amended or overturned, the Board must examine whether the approval of biddable tolls for FT-NR results in unjust discrimination. In that regard, it is necessary to consider sections 62, 63 and 67 of the Act. Those sections provide as follows:

> 62. All tolls shall be just and reasonable, and shall always, under substantially similar circumstances and conditions with respect to all traffic of the same description carried over the same route, be charged equally to all persons at the same rate.
>
> 63. The Board may determine, as questions of fact, whether or not traffic is or has been carried under substantially similar circumstances and conditions referred to in section 62, whether in any case a company has or has not complied with the provisions of that section, and whether there has, in any case, been unjust discrimination within the meaning of section 67.

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7 Subsection 60(1) of the Act provides: "A company shall not charge any tolls except tolls that are (a) specified in a tariff that has been filed with the Board and is in effect; or (b) approved by an order of the Board."

> 67. A company shall not make any unjust discrimination in tolls, service or facilities against any person or locality.

As a result of these provisions, different tolls can only be justified if they are in respect of: (i) traffic of differing descriptions; (ii) traffic carried over different routes; or, (iii) traffic transported under differing circumstances and conditions.[8]

Accordingly, in the Board's view, the first question to be decided is whether FT with a step-down and FT-NR are similar traffic. Parties' arguments in this regard centered on whether FT with a step-down and FT-NR are traffic of the same description transported under substantially similar circumstances and conditions.

The phrase "under substantially similar circumstances and conditions with respect to all traffic of the same description" was interpreted by the Board in the RH-1-88 Phase II Decision[9] to require that the Board consider all relevant matters affecting the traffic of the commodity by a pipeline. As the Board has exclusive authority under section 63 of the Act to determine, as questions of fact, whether or not traffic is or has been carried under substantially similar circumstances and conditions and whether there has been any unjust discrimination, the Board has broad discretion in determining what matters are relevant and what weight should be assigned to each in making its determination.

The Board finds that FT with a step-down and FT-NR are traffic of the same description transported under substantially similar circumstances and conditions. The evidence before the Board is that the services have the same features and are substitutable. The Board continues to ascribe to the view set out in its RH-1-89 Decision[10] that the intent of section 62 is that there must be compelling reasons to lead it to conclude that a service is not being provided under substantially similar circumstances and conditions. In the Board's view, the fact that there is a greater administrative burden associated with FT with a step-down is not sufficient to find that the services constitute different traffic.

In the RH-1-88 Phase II Decision, the Board stated:

> while the Board may take into account the business motives of the parties or the circumstances and conditions created by contract or any other matter that the Board considers

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8 See GH-2-87, TransCanada PipeLines Limited, Applications for Facilities and Approval of Toll Methodology and Related Tariff Matters, July 1988 at 72.

9 *Supra* note 6.

10 Westcoast Energy Inc., RH-1-89, Tolls, September 1989 at 27 to 28.

> relevant, it is for the Board alone to determine what weight should be given to such matters.[11]

Accordingly, the Board agrees with TransCanada that it is entitled to consider the business motives of the parties or the circumstances and conditions created by contract. The Board is not persuaded, however, that the services constitute different traffic because FT with a step-down was an interim solution to be used while the FT-NR service was being litigated. The Board is of the view that minimal weight can be assigned to this factor given TransCanada's evidence in the Phase I Proceeding as to the possibility of offering FT with a step-down service in the future. Further, the evidence of CAPP and Coral and CA in the Phase I Proceeding that the FT-NR service was unnecessary, and the position taken by CAPP on this review, suggests that not all parties were of the same understanding with respect to the interim nature of the FT with a step-down service offering.

Having determined that FT with a step-down and FT-NR constitute similar traffic, the second question to be decided is whether the original Panel should have considered the FT with a step-down toll as a comparator when setting tolls for FT-NR, notwithstanding the lack of discussion at the Phase I Proceeding on this issue and despite the fact that the FT toll for step-down service had not received Board approval.

The Board recognizes that no party raised the issue of the comparability of the toll charged for FT with a step-down service and the FT-NR toll in the Phase I Proceeding. However, evidence was on record as to the existence of FT with a step-down service being offered at the FT toll and as to the nature of the two services.

Further, the Board notes that TransCanada offered FT with a step-down service following discussions with its shippers. No shipper complained to the Board that the service offering was inconsistent with TransCanada's tariff or that Board approval was required. On this review, TransCanada, CAPP and Coral took the position that TransCanada had the discretion to amend the *pro forma* FT contract to include a step-down to zero volumes and to charge the FT toll for this service. In the Board's view, amending the *pro forma* contract in this manner, while not clearly prohibited, could be seen as being contrary to the spirit of the Board approved tariff. However, absent clear evidence that TransCanada's actions were in violation of the tariff or other regulatory authority, the Board is reluctant to find that a toll for a service which is already being charged pursuant to contracts is invalid.

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11 *Supra* note 6 at 48.

The Board is of the view that in the circumstances of this case, the original Panel should have had regard to the toll charged for the existing FT with a step-down service when setting the just and reasonable toll for FT-NR. The two services, FT with a step-down and FT-NR, constitute traffic of the same description transported under substantially similar circumstances and conditions. Accordingly, the original Panel erred by approving a toll methodology for FT-NR that could result in a different toll being charged for FT-NR than that in use for FT with a step-down.

TransCanada argued that the filed FT with a step-down toll should not trump the adjudicated FT-NR toll. The Board rejects this argument since it has found that the FT-NR toll was not properly adjudicated in the Phase I Proceeding.

The portion of the Phase I Decision which relates to the tolling of FT-NR is therefore overturned. Given the Board's findings on this review, the toll for FT-NR is to be calculated using the same methodology as for FT with a step-down. The Board's decisions regarding the approval of the FT-NR service and the filing of a report on this service by 1 November 2006 were not the subject of the review and remain unchanged.

Decision

The RH-2-2004 Phase I Decision authorizing FT-NR to be tolled on a biddable basis is overturned. The FT-NR service is to be tolled using the same methodology as for FT with a step-down.

Chapter 3

Regulatory Costs

In the Board's letter dated 18 February 2005, the Board dismissed the CAPP application on the regulatory costs ground of review on the basis that CAPP had not raised a doubt as the correctness of that decision. For convenience, the Board's reasons are repeated below.

Position of CAPP

In its review application, CAPP alleged that the Board erred by allowing TransCanada to recover, through tolls, regulatory and legal costs related to TransCanada's application to review the RH-4-2001[12] Board Decision and subsequent appeal of the RH-R-1-2002[13] Decision. CAPP submitted that TransCanada should not be permitted to recover regulatory and litigation costs which are incurred to increase returns to shareholders. CAPP further argued in reply that the Board erred in considering the reasonableness of such costs solely from the perspective of TransCanada without considering reasonableness from the perspective of TransCanada's tollpayers.

Positions of Parties in Support of CAPP

IGUA submitted that costs are reasonably and prudently incurred when the utility demonstrates that the costs were incurred to serve the interests of the utility and its tollpayers. In IGUA's submission, there was no evidence that the costs incurred for the review application and appeal were incurred to enhance the interests of TransCanada's tollpayers. Accordingly, the Board misapplied the reasonably and prudently incurred test.

None of the other parties supporting CAPP's application commented specifically on this issue.

Position of TransCanada

TransCanada disputed that regulatory and litigation costs should only be recoverable if they are expended to meet a Board requirement, noting that this argument was before the Board in the RH-2-2004 proceeding.

> ***Views of the Board***
>
> In the Board's view, the Panel considering this issue had the discretion to determine whether these costs should be included in TransCanada's tolls. The Panel clearly established the principles which should be used when determining whether a company is entitled to recover regulatory costs; found that the expenses were an integral and legitimate cost of doing

12 TransCanada PipeLines Limited, RH-4-2001, Cost of Capital, June 2002.

13 *Supra* note 5.

business; and decided that the costs were incurred in a manner which accorded with the principles. Thus, it is evident that the Panel addressed its mind to what the appropriate test should be in determining whether to include the costs, and having considered the evidence, properly applied that test. While it is clear that CAPP disagrees with this decision, the decision was within the Board's discretion. The Board is of the view that CAPP has not raised a doubt as to the correctness of the Phase I Decision with respect to regulatory costs.

Chapter 4

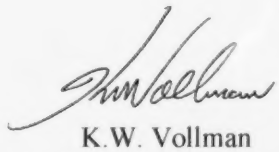
LTIC

In its application, CAPP alleged that the Board erred in allowing TransCanada to include all forecast LTIC costs in its 2004 cost of service. By letter dated 11 February 2005, CAPP requested that the Board defer its consideration of the LTIC issue pending further advice. The LTIC ground of review was subsequently withdrawn by CAPP on 13 April 2005. Accordingly, the Board is of the view that no further consideration of this ground of review is required.

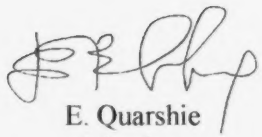
Chapter 5

Disposition

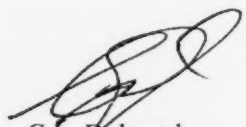
The foregoing chapters and Order AO-4-TGI-07-2003 constitute the Board's Decision and Reasons for Decision in respect of the CAPP application to review the RH-2-2004 Phase I Decision.



K.W. Vollman
Presiding Member



E. Quarshie
Member



C.L. Dybwad
Member

Calgary, Alberta
May 2005

Appendix I

Order AO-4-TGI-07-2003

ORDER AO-4-TGI-07-2003

IN THE MATTER OF the *National Energy Board Act* and the regulations made thereunder; and

IN THE MATTER OF Board Decision RH-2-2004 Phase I; and

IN THE MATTER OF an application filed by the Canadian Association of Petroleum Producers for Review of Board Decision RH-2-2004 Phase I; and

IN THE MATTER OF Proceeding RH-R-1-2005.

BEFORE the Board on 18 May 2005.

WHEREAS TransCanada filed an application dated 12 November 2003 for interim tolls for the Mainline effective 1 January 2004;

AND WHEREAS on 18 December 2003, the Board approved TransCanada's 12 November 2003 application, as amended on 3 December 2003, and issued Order TGI-07-2003;

AND WHEREAS TransCanada filed an application dated 26 January 2004 for an order fixing just and reasonable tolls that it may charge for or in respect of transportation services provided on its Mainline between 1 January 2004 and 31 December 2004 (2004 Tolls Application);

AND WHEREAS on 23 March 2004, the Board issued Hearing Order RH-2-2004 establishing a two-phase procedure to consider TransCanada's 2004 Tolls Application;

AND WHEREAS on 23 July 2004, the Board issued Amending Order AO-1-TGI-07-2003 approving revised interim tolls effective 1 August 2004;

AND WHEREAS the Board held oral public hearings with respect to RH-2-2004 Phase I and Phase II matters;

AND WHEREAS the Board's Decisions arising out of the RH-2-2004 Phase I Proceeding are set out in its Reasons for Decision dated September 2004, and in Order AO-2-TGI-07-2003;

AND WHEREAS the Board's Decisions arising out of the RH-2-2004 Phase II Proceeding are set out in its Reasons for Decision dated April 2005, and in Order AO-3-TGI-07-2003;

AND WHEREAS on 11 January 2005, Coral Energy Canada Inc. (Coral) and the Cogenerators Alliance (CA) filed an application for a review and variance of the RH-2-2004 Phase I Decision;

AND WHEREAS in its RH-R-2-2005 Reasons for Decision dated May 2005, the Board dismissed the Coral and CA application for review and variance of the RH-2-2004 Phase I Decision dated 11 January 2005;

AND WHEREAS on 12 November 2004, the Canadian Association of Petroleum Producers (CAPP) filed an application for a review of the RH-2-2004 Phase I Decision;

AND WHEREAS by letter dated 15 December 2004, the Board established a process to solicit comments on the threshold question of the CAPP review as to whether CAPP had raised a doubt as the correctness of the RH-2-2004 Phase I Decision such that it ought to be reviewed;

AND WHEREAS on 18 February 2005, the Board issued a letter in which it found that CAPP had raised a doubt as to the correctness of the Board's decision with respect to Non-Renewable Firm Transportation (FT-NR);

AND WHEREAS on 18 March 2005, the Board set down for oral public hearing Proceeding RH-R-1-2005 to address the question raised by CAPP as to whether the Board had erred in the RH-2-2004 Phase I Decision by approving a different toll for FT-NR than the toll charged for Firm Transportation (FT) with a step-down;

AND WHEREAS an oral public hearing was held in Calgary, Alberta on 26 April 2005 during which time the Board heard argument with respect to whether the RH-2-2004 Phase I Decision regarding the tolling of FT-NR should be confirmed, amended or overturned and how FT-NR should be tolled in the event the RH-2-2004 Phase I Decision were to be amended or overturned;

AND WHEREAS in its RH-R-1-2005 Reasons for Decision May 2005, the Board determined that the RH-2-2004 Phase I Panel had erred by approving a toll methodology for FT-NR that could result in a different toll being charged for FT-NR than that in use for FT with a step-down;

THEREFORE, IT IS ORDERED, pursuant to Parts I and IV of the Act, that:

The toll charged for FT-NR shall be calculated using the same tolling methodology as for FT with a step-down.

NATIONAL ENERGY BOARD

Michel L. Mantha
Secretary